

# **Audit of USAID/Peru's Recipient Audit Inventory**

**Audit Report No. 1-527-02-010-P**

**May 8, 2002**

**Regional Inspector General / San Salvador**



U.S. AGENCY FOR  
INTERNATIONAL  
DEVELOPMENT

*RIG/San Salvador*

May 8, 2002

**MEMORANDUM**

**FOR:** USAID/Peru Director, Thomas Geiger

**FROM:** Acting Regional Inspector General/San Salvador,  
Steven H. Bernstein

**SUBJECT:** Audit of USAID/Peru's Recipient Audit Inventory (Report No.  
1-527-02-010-P)

This is our final report on the subject audit. In finalizing the report, we considered your comments on the draft report, which are included in their entirety in Appendix II.

This report includes two recommendations for your action. Final action has been taken on Recommendation Nos. 1 and 2, and these recommendations are closed upon issuance of this audit report.

I appreciate the assistance and cooperation provided to the audit staff on this assignment.

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**Summary of Results**

The Regional Inspector General/San Salvador performed an audit to determine whether USAID/Peru's audit inventory is complete and accurate, and whether the required audits were performed in a timely manner. (See pages 3 and 4).

USAID/Peru's fiscal year 2002 audit inventory was accurate. However, the audit inventory was not complete, since 20 awards (or 17 per cent) that should have been included in the audit inventory were not included. The audits were not done in a timely manner, since out of the 27 audits that should have been submitted by September 30, 2001, 23 were submitted late, and 2 were not submitted by the end of our field work. (See pages 4 through 7).

USAID/Peru was in general agreement with the findings and recommendations in the report. (See pages 7 through 8).

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**Background**

Financial audits of contracts and grants are a primary basis for effective management and control of USAID's program expenditures. These audits are designed to provide USAID management reasonable assurance that transactions are properly recorded and accounted for; laws and regulations, and provisions of contract or grant agreements are complied with; and USAID-financed funds, property, and other assets are safeguarded against unauthorized use or disposition.

Automated Directives System Chapter 591, updated January 2002, requires USAID missions to (1) establish an audit management plan; (2) maintain an audit inventory database; and (3) have audits done for non-U.S. grants, contracts, and cooperative agreements that meet the audit threshold.

In May 1999, Office of Inspector General management decided to verify the accuracy of USAID missions' recipient audit inventory worldwide over a period of three years because the lack of audit coverage was perceived as a high-risk area.

Our audit covered \$155.7 million in USAID/Peru disbursements.

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**Audit Objective**

As part of its fiscal year 2001 audit plan, the Regional Inspector General/San Salvador performed an audit to answer the following question:

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- Is USAID/Peru's audit inventory complete and accurate, and were the required audits done in a timely manner?

The audit scope and methodology is presented in Appendix I.

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## **Audit Findings**    **Is USAID/Peru's audit inventory complete and accurate, and were the required audits done in a timely manner?**

USAID/Peru's fiscal year 2002 audit inventory was accurate. However, the audit inventory was not complete. Moreover, required audits were not submitted in a timely manner.

USAID/Peru took several positive steps to implement and manage the recipient-contracted audit program. These steps included:

- Incorporating appropriate provisions into contracts, grants, and cooperative agreements that require recipients to arrange audits whenever the recipients spend \$300,000 or more in USAID funds during their fiscal year.
- Maintaining an inventory of contracts, grants, and cooperative agreements requiring audits and maintaining an audit plan to track planned audits.
- Circulating the audit inventory to mission technical offices so that mission staff with first hand knowledge of the activities could verify that the audit inventory was accurate and complete.
- Establishing a Management Control Review Committee that has begun to monitor implementation of the recipient-contracted audit program.
- Designating an Audit Management Officer to coordinate and monitor the recipient-contracted audit program and coordinate follow-up on audit recommendations.

USAID/Peru's fiscal year 2002 audit inventory was accurate. We reviewed a random sample of 70 of the 680 individual data items in the audit inventory and found two errors. One of the errors pertained to an entity (the Instituto de Diálogo y Propuesta) that spent \$419,136 in USAID funds and was not scheduled to be audited, even though this amount exceeded the \$300,000 threshold established by USAID policy.<sup>1</sup> The second error was that the completion date for one grant was incorrect.

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<sup>1</sup> We are not making a recommendation on this issue, since in August 2001 the recipient started the audit firm selection process.

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Based on the information in the preceding paragraph, the observed error rate in our sample was 2.8 percent. The sample design provided 90 percent confidence that the error rate in the population of all 680 data items was below 5 percent (see Appendix I).

However, the fiscal year 2002 audit inventory was not complete and most audits were not done on time. These problems are discussed in the following sections.

### **Audit Inventory Was Not Complete**

Section 591.3.4.2.a. of USAID's Automated Directive System (ADS) requires that missions maintain an inventory of all contracts, grants, and cooperative agreements. For entities that do not require audit, missions must annotate the specific reason that no audit is required. This practice – including all awards in the inventory and then annotating specific reasons where no audit is required – helps prevent errors and provides a more complete record of the process followed to develop the annual audit plan.

Ninety-seven contracts, grants, and cooperative agreements were included in the audit inventory.<sup>2</sup> We reviewed a list of actions signed by the regional contracting officer and found 20 awards that should have been included in the audit inventory, but were not. In other words, 17 percent of the awards that should have been included in the audit inventory were excluded. The total commitment amount excluded from the audit inventory was \$2.7 million, or about 1 percent of the total \$339 million in commitments that should have been included in the audit inventory.

There were several reasons why some awards were not included in the audit inventory:

- Mission staff excluded some small awards from the final audit inventory because they considered the award amounts to be inconsequential. While this reasoning is understandable, the ADS section cited above requires that all awards be included in the audit inventory to help minimize the possibility of error and help document the process used to prepare the final audit plan.
- The mission used source information extracted from the Mission Accounting and Control System (MACS). Using a spreadsheet program, staff sorted the data several times to separate U.S. from non-U.S. recipients and removed purchase orders, personal services contracts, and other types of agreements that do not have to be included in the final audit inventory. These sorting

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<sup>2</sup> The 97 contracts, grants and cooperative agreements consisted of 26 U.S. and 71 non-U.S. contractors, international organizations, and grantees. The 680 data elements mentioned in the prior page refer to the 71 non-U.S. recipients, since the ADS does not specify the data elements necessary for U.S. recipients. The 680 data elements consist of 68 rows with 10 columns each, and one row does not necessarily correspond to one award given the manner that the data is organized.

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operations sometimes resulted in records being accidentally removed for reasons that we could not determine after the fact.

- To help maintain the integrity of the information used to prepare the audit inventory, staff endeavored to compare the total commitment amounts in the audit inventory to the total commitment amounts in the source file every time the information was sorted or otherwise modified. However, this control technique – verifying commitment amounts through comparison with the source MACS report – was not consistently followed throughout the process. Therefore, it was difficult to know when awards were deleted from the inventory.

Whenever awards are excluded from the audit inventory, mission management is placed in the position of making decisions based on incomplete information, and the possibility is introduced that audits may not be planned or performed that otherwise would have been. Because most of the awards excluded from the audit inventory were relatively small (below the \$300,000 audit threshold) – ranging in size from \$1,500 to \$184,230 – in most cases this possibility was relatively negligible. However, in one case, a \$1.8 million award – to the Asociación de Municipalidades del Valle Rio Apurimac y Ene – was inadvertently excluded from the audit inventory, resulting in an audit not being planned that was required by USAID policy. (In addition, as stated on page 4, another award was included in the audit inventory but not scheduled for audit even though an audit was required by USAID policy.)

**Recommendation No. 1: We recommend that USAID/Peru:**

- 1.1 implement controls that provide reasonable assurance that all contracts, grants, and cooperative agreements are included in the audit inventory; and**
- 1.2 schedule an audit of the Asociación de Municipalidades del Valle Rio Apurimac y Ene.**

**Required Audits Were Not  
Done in a Timely Manner**

Chapter 591 of the ADS requires missions to establish an audit management plan to ensure complete audit coverage of their non-U.S. grantees and contractors. In addition, OIG's *Guidelines for Financial Audits Contracted by Foreign Recipients* states that reports resulting from these audits are to be submitted to the cognizant Regional Inspector General audit office within nine months after the recipient's fiscal year-end for review and release.

Based on the audit inventory, there were 27 audits that should have been submitted to the Regional Inspector General/San Salvador during fiscal year

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2001. Two of the 27 audit reports were submitted to the Regional Inspector General/San Salvador within the required nine-month timeframe. Twenty-three audit reports were submitted late<sup>3</sup> and two audit reports<sup>4</sup> still had not been submitted by the end of our audit fieldwork on February 15, 2002.

There were two principal reasons why audit reports were submitted late:

- Recipients typically did not arrange for audits until after the end of the year to be audited. This precluded the possibility of performing interim audit work during the year to speed completion of the audit and issuance of the audit report after the end of the year.
- Audits sometimes took an inordinate amount of time to complete because the auditors and auditees were unable to resolve issues involving access to records, scheduling audit work, and disagreements over audit findings without intervention by USAID/Peru. Because we discussed this situation in detail at the exit conference, we are making no recommendation addressing this cause.

Because required audits were not completed in a timely manner, USAID/Peru did not have adequate assurance that: (1) audits of non-U.S. recipients were conducted in accordance with USAID requirements, and (2) the recommendations were timely tracked in USAID's Consolidated Audit Tracking System. As a result of the above, we are making the following recommendation:

**Recommendation No. 2: We recommend that USAID/Peru:**

- 2.1 as a one-time measure to catch up on audits that are late, require recipients to arrange single audits to cover all periods that have not yet been audited in conjunction with the audits of the current year; and**
- 2.2 require that recipients sign audit contracts no later than six months before the end of the year to be audited.**

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**Management  
Comments  
and Our  
Evaluation**

USAID/Peru was in general agreement with the findings and recommendations in the report.

In response to part 1.1 of Recommendation No. 1, USAID/Peru instituted controls to ensure that future audit inventories include all grants, cooperative agreements,

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<sup>3</sup> Of the 23 reports, 3 were up to 90 days late, 14 were from 91 to 365 days late, and 6 were over a year late.

<sup>4</sup> In one of the two cases, an audit report was submitted to RIG/San Salvador. However, after this office performed a quality control review of the audit firm, the report was deemed unacceptable. A report by a different audit firm has not been submitted yet.



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and contracts, as required, and that the audit inventory will be appropriately annotated whenever a particular award is not subject to audit in a given year. Such controls include the reconciliation of the audit inventory with the total universe of commitments per the Mission Accounting Control System (MACS) records. With respect to part 1.2 of Recommendation No. 1, USAID/Peru has asked the recipient to initiate the audit that had been omitted from the FY2002 inventory, and contracting for such audit is now underway.

In response to part 2.1 of Recommendation No. 2, USAID/Peru has arranged with all recipients concerned, as a one-time measure, for a single catch-up audit to be performed covering all prior periods yet to be audited in conjunction with the audit of the current year. With respect to part 2.2 of Recommendation No. 2, USAID/Peru has instituted a new policy requiring that a letter be sent to each recipient subject to audit six months before the end of the year to be audited, recommending that the audit be contracted for without delay. Although technically this new policy does not directly follow our recommendation, in considering the mission comments, we agree this is a suitable response to our recommendation.

Based on the above, final action has been taken on Recommendation Nos. 1 and 2, and these recommendations are closed upon issuance of this audit report.

## Scope and Methodology

### Scope

The audit was performed in accordance with generally accepted government auditing standards. The audit assessed (1) whether USAID/Peru's audit inventory for fiscal year 2002 was complete and accurate, and (2) whether required audits for fiscal year 2001 were performed in a timely manner. In assessing whether the audit inventory was complete and accurate, we reviewed the fiscal year 2002 inventory since this was the most recent audit inventory prepared by USAID/Peru. In assessing whether required audits were completed in a timely manner, we reviewed the audits listed in the fiscal year 2001 inventory, since the audits listed in the fiscal year 2002 inventory were not yet due at the time of our audit.

Fieldwork was performed at USAID/Peru from February 11 through February 15, 2002 and covered a total of \$155.7 million in USAID funds.

We obtained an understanding of the management controls related to the audit objective and assessed risk exposure and control effectiveness. The specific control techniques we assessed were the following:

- Including appropriate audit provisions in contracts, grants, and cooperative agreements.
- Verifying whether the commitment totals in the audit inventory were the same as the commitment totals in the source report drawn from the Mission Accounting and Control System (MACS).
- Circulating the audit inventory to mission technical offices so that mission staff with first hand knowledge of the activities could verify that the audit inventory was accurate and complete.
- Establishing a Management Control Review Committee that, beginning with a meeting held in January 2002, has begun to monitor implementation of the recipient-contracted audit program.
- Designating an Audit Management Officer to coordinate and monitor the recipient-contracted audit program and coordinate follow-up on audit recommendations.

The audit scope included:

- Reviewing the mission's audit inventories and related documents.

- Interviewing cognizant mission officials.
- Reviewing the mission's automated database inventory of contracts, grants, and cooperative agreements and identifying those that require audits.
- Comparing information in the audit inventory with other available sources of information as discussed in the following section.

The audit criteria was principally comprised of Chapter 591 of USAID's Automated Directives System, revised January 2002, and the OIG's "*Guidelines for Financial Audits Contracted by Foreign Recipients*".

We did not audit the accuracy of the information in the mission's MACS database system because of time constraints and because it was not directly relevant to our audit objective.

### Methodology

To assess whether the audit inventory was complete and accurate, we obtained the fiscal year 2002 audit inventory and performed comparisons between the information in the audit inventory and other available sources of information. We considered error rates of 5 percent or more to be significant. (This threshold reflects our judgments about the level of performance that is reasonable and attainable for this part of the audit objective.)

To verify the accuracy of information in the audit inventory, we drew a random sample of 70 of 680 individual data items in the audit inventory. We verified these items by:

- Tracing grantee names, agreement numbers, agreement amounts, and agreement start and end dates to agreements and implementation letters.
- Reviewing MACS reports to verify whether or not expenditures by recipients exceeded the \$300,000 audit threshold.
- Reviewing audit reports to verify the dates and coverage of audits listed in the audit inventory.
- Interviewing financial analysts to verify that no previous audits were performed where none were listed in the audit inventory.

Given the observed error rate in our sample of 2.8 percent (see page 5), the sample design provided 90 percent confidence that the error rate in the sample would be representative of the error rate in the entire population of all 680 data items with precision of plus or minus 5 percent.

We determined whether the information in the audit inventory was complete by:

- Obtaining from the regional contracts office a listing of all contracts, grants, and cooperative agreements signed by the regional contracting officer that were active during calendar year 2001 and verifying that each of these agreements was included in the fiscal year 2002 audit inventory.
- Obtaining a listing of disbursements from MACS to verify that all entities that received USAID/Peru disbursements of \$300,000 or more during calendar year 2001 were included in the fiscal year 2002 audit inventory.

To determine whether required audits for fiscal year 2001 were submitted in a timely manner, we obtained the fiscal year 2001 audit inventory. We tested 100 percent of the 30 scheduled audits in the fiscal year 2001 audit inventory. Specifically, we verified timeliness by reviewing RIG/San Salvador logs pertaining to those audits, as well as files held by the financial analysts at the Comptroller's Office, to see whether required audits listed in the audit inventory were submitted to the OIG and if so, when. We considered error rates of 10 percent or more to be significant and reportable. (This threshold reflects our judgments about the level of performance that is reasonable and attainable for this part of the audit objective.)

**Management  
Comments**

***Memorandum***

**TO :** Timothy Cox, Regional Inspector General/San Salvador

**FROM:** Thomas L. Geiger, Mission Director, USAID/Peru (signed in original)

**DATE:** April 6, 2002

**SUBJECT:** Audit of USAID/Peru's Recipient Audit Inventory Draft Report No. 1-527-02-xxx-P

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Please find below USAID/Peru's comments to the subject draft audit report:

USAID/Peru agrees with RIG/SS audit findings regarding the lack of completeness of USAID/Peru's fiscal year 2002 audit inventory and the late submission of audit reports related to recipient-contracted audits.

With respect to completeness, we have coordinated with the recipient concerning initiation of the audit that had been omitted from FY2002 audit inventory and contracting for the required audit is now underway. In addition, we have instituted controls to ensure that future audit inventories include all grants, cooperative agreements, and contracts, as required, and that the audit inventory will be appropriately annotated whenever a particular award is not subject to audit in a given year. Such controls include the reconciliation of the audit inventory with the total universe of commitments per the Mission Accounting Control System (MACS) records.

With respect to the timeliness of audits, we have arranged with all recipients concerned, as a one-time measure, for a single catch-up audit to be performed covering all prior periods yet to be audited in conjunction with the audit of the current year. This action will bring USAID/Peru's recipients fully up-to-date in audit compliance by the end of 2002. Furthermore, to help ensure that future audits are completed on a timely basis, USAID/Peru has instituted a new policy requiring that a letter be sent to each recipient subject to audit 6 months before the end of the year to be audited recommending that the audit be contracted for without delay to begin the audit process.

Based on the above described actions taken to date by USAID/Peru, we request recommendation that recommendations No.1 and 2 of subject draft audit report be closed upon final issuance.

We would like to thank you and your staff for the collaborative manner in which this audit was conducted, and to make my staff and myself available for any additional information or documentation needed for the successful closure of the audit recommendations.